

No. 15503

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In the United States Court of Appeals  
for the Ninth Circuit

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ESTATE OF GRACE N. WILLIAMS, DECEASED, RALPH  
E. WILLIAMS, EXECUTOR, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

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On Petition for Review of the Decision of the  
Tax Court of the United States

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BRIEF FOR THE RESPONDENT

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**OPINION BELOW**

The memorandum findings of fact and opinion of the Tax Court (R. 112-119) are not officially reported.

**JURISDICTION**

This petition for review (R. 121-126) involves federal income taxes for the taxable years 1951 and 1952 (R. 112). The Commissioner mailed to taxpayer on February 3, 1955 (R. 26), a notice of deficiency in income taxes in the amount of \$2,806.69 for 1951 and in the amount of \$13,060.19 for 1952

(R. 17). Taxpayer filed a timely petition for redetermination with the Tax Court under the provisions of Section 272(a)(1) Internal Revenue Code of 1939. (R. 3, 5, 25.) The decision of the Tax Court was entered on December 12, 1956. (R. 120.) A timely petition for review by this Court was filed on March 7, 1957. (R. 4.) Jurisdiction is conferred on this Court by Section 7482, Internal Revenue Code of 1954.

### QUESTION PRESENTED

Whether the record supports the finding of the Tax Court that the fair market value of the growing hops involved was \$11,500 on July 31, 1952, on which date taxpayer acquired the hops as a liquidating dividend?

### STATUTES AND REGULATIONS

Internal Revenue Code of 1939:

SEC. 111. DETERMINATION OF AMOUNT OF, AND RECOGNITION OF, GAIN OR LOSS.

(a) *Computation of Gain or Loss.*—The gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the adjusted basis provided in section 113 (b) for determining gain, and the loss shall be the excess of the adjusted basis provided in such section for determining loss over the amount realized.

(b) *Amount Realized.*—The amount realized from the sale or other disposition of property shall be the sum of any money received plus

the fair market value of the property (other than money) received.

(c) *Recognition of Gain or Loss.*—In the case of a sale or exchange, the extent to which the gain or loss determined under this section shall be recognized for the purposes of this chapter, shall be determined under the provisions of section 112.

\* \* \* \*

(26 U.S.C. 1952 ed., Sec. 111.)

## SEC. 112. RECOGNITION OF GAIN OR LOSS.

(a) *General Rule.*—Upon the sale or exchange of property the entire amount of the gain or loss, determined under section 111, shall be recognized, except as hereinafter provided in this section.

\* \* \* \*

(26 U.S.C. 1952 ed., Sec. 112.)

Treasury Regulations 111, promulgated under the Internal Revenue Code of 1939:

Sec. 29.111-1. *Computation of Gain or Loss.*  
—Except as otherwise provided, the Internal Revenue Code regards as income or as loss sustained, the gain or loss realized from the conversion of property into cash, or from the exchange of property for other property differing materially either in kind or in extent. The amount realized from a sale or other disposition of property is the sum of any money received plus the fair market value of any property which is received. The fair market value of property is a question of fact, but only in rare and extraordinary cases will property be considered to have no fair market value. \* \* \*



Treasury Regulations 118, promulgated under the Internal Revenue Code of 1939:

Sec. 39.111-1 *Computation of gain or loss.*

(a) Except as otherwise provided, the Internal Revenue Code regards as income or as loss sustained, the gain or loss realized from the conversion of property into cash, or from the exchange of property for other property differing materially either in kind or in extent. The amount realized from a sale or other disposition of property is the sum of any money received plus the fair market value of any property which is received. The fair market value of property is a question of fact, but only in rare and extraordinary cases will property be considered to have no fair market value. \* \* \*

Sec. 39.112 (a)-1 *Sales or exchanges.* (a)

The extent to which the amount of gain or loss, determined under section 111, from the sale or exchange of property is to be recognized is governed by the provisions of section 112. The general rule is that the entire amount of such gain or loss is to be recognized.

\* \* \* \*

## STATEMENT

The facts as found by the Tax Court, some of which were stipulated, may be summarized as follows:

Prior to 1950, the Eola Hop Farms located in Marion County, Oregon, had been owned and operated by Grace N. Williams (hereinafter referred to as the decedent) and a co-partner, under the part-



nership name of Williams and Thacker. Of its approximately 165 acres, 149.5 acres were planted to hops. In 1950, the interest of the co-partner was purchased by the decedent and thereafter until March 1, 1951, decedent operated the business as a sole proprietorship. On March 1, 1951, all of the assets and liabilities of the sole proprietorship were transferred by decedent to Eola Hop Farms, Inc., a corporation, in exchange for all of the capital stock of the corporation. From March 1, 1951, to July 31, 1952, the farming business was carried on by the corporation. Thereafter, farming operations were carried on by decedent as a sole proprietorship. In 1953, the hop vines were pulled up and the growing of hops abandoned. (R. 112-113.)

The receipts from the sale of hops for the years 1950, 1951 and 1952 and the expenses incurred attributable to such receipts are as follows:

Year	Reported Hop Receipts	Reported Expenses
1950.....	\$108,246.42	\$85,820.81
1951.....	88,506.31	82,826.96
1952.....	46,445.72	86,181.55

The total crop production for 1952, in terms of pounds, the salable quantity of the crop, the amounts sold, and the unit price per pound received and the total receipts for the 1952 hops are shown by the following (R. 114):

#### 1952 Crop Hops

Total crop—per Hop Control Board.....	152,740 pounds
Salable percentage .....	<u>65.7 %</u>
Salable allotment.....	100,350 pounds

Sales	Bales	Pounds	Price	Amount
Jos. Schlitz Brewing Co.....	246	48,716	52¢	\$25,332.32
Hans Hinrichs Hops Co., Inc.	32	7,643	67¢	5,120.81
Paul Reinemann Co.....	1	228	42¢	95.76
Paul Reinemann Co.....	13	2,399	42¢	1,007.58
Yakima Chief Ranches, Inc..	226	45,697	34¢	15,536.98
	518	104,683		\$47,093.45
Certificate purchase .....		2,399	27¢	647.73
	518	102,284		\$46,445.72

No contracts for the sale of the 1952 hop crop to dealers or users or any other persons had been executed by either the corporation or the decedent as of July 31, 1952. (R. 114.)

The average cost of planting and cultivating on lands in the vicinity of the Eola Farms during the year 1952 was from 22 to 25 cents per pound and the average cost of harvesting and baling was from 20 to 25 cents per pound. (R. 115.)

The growing crop of hops distributed to the decedent was not matured on July 31, 1952, and the risk of loss from mildew and other crop diseases was practically non-existent at that date. The crop matured during the latter part of August and the early part of September of 1952. (R. 115.)

The average market price for the type of hops grown on the Eola Farms as of July 31, 1952, was between 49 and 52 cents per pound. In the latter part of August the price range was between 30 and 35 cents per pound. In the middle of October the market became more active and through November ranged from 45 to 50 cents per pound and during December the price ranged from 50 to 53 cents per pound. (R. 115.)

The hop industry has been suffering from serious overproduction since 1950. The market, for the most part of 1952, was relatively inactive. Under the Agriculture Market Agreement Act of 1937, the industry put into effect an agreement providing the industry with authority to bring supplies in balance with demand. The agreement was administered by a Hop Control Board made up of growers, dealers, brewers and Government representatives. The Board met in the late summer of each year and made a survey of prospective demands and other factors which might effect market conditions. It determined what they considered to be the salable quantity of crop then planted—a quantity which the trade could consume and which would reflect a fair return to the grower. The Board made a recommendation as to salable quantity which was transmitted to the Secretary of Agriculture for final decision. The Secretary considered the recommendation of the Board, along with other pertinent data, and issued a final salable quantity. In general, the Board's recommendation as to the salable quantity was adopted by the Secretary without substantial change. In the year 1952, the Board's recommendation did not vary more than one or two per cent from the final decision made by the Secretary of Agriculture. (R.115-116).

The overall salable quantity for the hop industry determined by the Secretary was a percentage of each growers' crop and the growers could not market more than such established percentage. Nevertheless, it was necessary for each grower to harvest

all his crop, including the unsalable portion. (R. 116).

The salable percentage of each grower's crop was slightly in excess of 85 per cent in 1950; approximately 74 per cent in 1951; and in 1952 it was 65.7 per cent. (R. 116.)

The Hop Control Board met on July 17, 1952, and made its recommendation to the Secretary of Agriculture as to the salable quantity of the crop for that year. (R. 116-117.)

R. E. Williams, Jr., a son of decedent and executor of her estate, had long been active as a grower and dealer in hops. He was a member of the Hop Control Board and in 1952 he participated in its deliberations which resulted in recommending that approximately 36 per cent of the crop be declared non-salable. Williams managed the Eola Farms in 1952 and had managed it since 1940. He handled the decedent's hop growing affairs in 1952 and for a considerable time prior thereto. He also participated in the decision to dissolve the corporation on July 31, 1952. (R. 117.)

The Eola Hop Farms corporation reported a loss of \$8,597.33 for its operations for the period from March 1, 1951, to December 31, 1951. For the seven months ending July 31, 1952, a loss was reported by the corporation in the amount of \$339.12; however, in the computation of such loss the expenses incurred by the corporation in planting hops in March and caring for the 1952 crop up to July 31, 1952, were not deducted but were carried on the balance sheet of the corporation as an asset in the amount of \$44,165.66. This sum was carried over

and utilized by the decedent in computing the loss attributable to the 1952 hop crop. In addition to the above expenses incurred by the corporation, the decedent, operating as a sole proprietor after July 31, 1952, incurred further harvesting and marketing expenses attributable to the hop crop in the amount of \$42,015.89. (R. 113.)

The net income reported by decedent for the year 1950 was \$36,241.51; for the year 1951, \$30,344.40. In her federal income tax return for 1952, decedent reported a net farm loss of \$43,385.90 on the operation at the Eola Farms. When this loss was offset against her other income, the result, as reported on her tax return, was a net loss of \$8,731.03. (R. 114-115.)

In computing the loss upon liquidation of the Eola Hop Farms corporation and the operating loss for 1952 (R. 20-22), the Commissioner determined that the fair market value of the crop as of July 31, 1952, was \$4,375.40. This amount was determined by deducting the total cost of the operations of the farm for the period August 1, 1952, to December 31, 1952, from the total farm revenue for the year 1952. (R. 118.) The Tax Court made the factual finding that the fair market value of the hop crop as of July 31, 1952, was \$11,500. (R. 117, 119.)

#### SUMMARY OF ARGUMENT

The question to be determined by this Court is whether the Tax Court's finding of the fair market value of growing hops on July 31, 1952, is clearly erroneous. This Court has consistently stated that



findings of value are purely questions of fact and that the decision of the Tax Court will not be set aside unless the decision is clearly erroneous. In arriving at its determination, the Tax Court considered the maturity of the crop, the risk of loss, the estimated yield, the market price of similar hops, the cost of harvesting, the salable quantity as restricted by the industry agreement, the special knowledge of buyers in the industry and expert testimony. These factors were correctly considered by the Tax Court in determining fair market value and there is ample evidence of record so that the Tax Court's finding cannot be said to be clearly erroneous.

### ARGUMENT

**The Record Fully Supports the Tax Court's Finding That the Fair Market Value of the Growing Hops Involved Was \$11,500 On the Critical Date of July 31, 1952**

Section 111, Internal Revenue Code of 1939, *supra*, provides for the determination of the amount of gain or loss in the case of a sale or exchange. Gain or loss is computed after determining the amount realized from the sale or exchange and the amount realized includes cash and the fair market value of property received. Section 111(a) and (b). The decedent here received property, i.e., the growing hops, as a liquidating dividend on July 31, 1952, in the exchange in question. (R. 117.) To determine the amount realized—in order to compute the loss resulting from the exchange here (R. 21-22)—the fair market value of the hops must be ascertained. Section 111(b). Whether the fair market value of the

hops as determined by the Tax Court is clearly erroneous is the sole issue here. (R. 112.)

It is well settled that "fair market value" is the price at which property would change hands between a willing buyer and a willing seller neither being under any compulsion to buy or sell. *Elmhurst Cemetery Co. v. Commissioner*, 300 U.S. 37, 39; *Olson v. United States*, 292 U.S. 246, 257. The question of fair market value is one of fact. *Simons Brick Co. v. Commissioner*, 45 F. 2d 57 (C.A. 9th), certiorari denied, 283 U.S. 834; *Commissioner v. Moore*, 207 F. 2d 265 (C.A. 9th). No single criterion is decisive but all relevant factors are considered. *Olson v. United States*, *supra*; *Penn v. Commissioner*, 219 F. 2d 18 (C.A. 9th). As this Court very recently stated (*Penn v. Commissioner*, *supra*, pp. 20-21):

The matter [of fair market value] is pure fact. The court has heard the evidence, considered the stipulated facts and exhibits and arrived at the value. There is no question upon which all persons, reasonable or otherwise, are so apt to differ as upon a question of value. It makes little difference whether the facts agreed upon or stipulated are in writing or by oral testimony. The duty of finding the facts is placed upon that court. When found, such facts are binding upon the appellate courts.

This is far from saying that the appellate court should refuse to recognize its responsibility to set aside a finding which is "clearly erroneous," especially when a firm conviction is arrived at that, considering the whole record, a



mistake has been committed. But the appellate court should never make the error of substituting its own judgment of the record as a whole for that of the findings of the tribunal primarily charged with the responsibility. It is a subtle difference, but a real one.

\* \* \* \*

If improper weight may have been given to these elements of evaluation but the conclusion was not demonstrably wrong, an appellate court should not interfere. Congress has committed questions such as valuation to the Tax Court. \* \* \*

Accordingly, respondent need only point out here the ample facts of record which support the Tax Court's finding.

The hop crop involved was planted in March of 1952. (R. 113.) It did not mature until the latter part of August and the early part of September, 1952. (R. 115.) Although on the critical date, July 31, 1952, the crop was not matured, the risk of loss from mildew and other diseases was practically nil so that the yield could be estimated. Especially significant concerning value is that, as of the critical date, no contract had been consummated for the sale of this crop. (R. 114, 118.)

Since 1950, the hop industry had been suffering from serious overproduction. For the most part of 1952, the market was relatively inactive. In order to bring supplies in balance with demand, the industry had in effect an agreement under the Agriculture Market Agreement Act of 1937. The agreement was administered by the Hop Control Board.

During the summer of each year, the Board made a survey of prospective demand and other factors which might affect market conditions. It determined the salable quantity of crops then planted and made a recommendation of salable quantity to the Secretary of Agriculture. In 1952, the Board made its recommendation to the Secretary on July 17. Usually, the Board's recommendation was adopted by the Secretary without substantial change; but the Secretary issued the final salable quantity. In 1952, the Board's recommendation was the same as that finally adopted.<sup>1</sup> (R. 105, 115-117.)

The industry's agreement limited each grower's salable crop to the percentage established by the Secretary. The grower could not market more than the established percentage although it was necessary to harvest all his crop. The salable percentage of each grower's crop was approximately 74 per cent in 1951 and 65.7 per cent in 1952. (R. 116.) Thus, approximately 35 per cent of decedent's crop involved was unsalable.

It was well known by the growers and users of hops that the Hop Control Board's recommendation did not vary much from the Secretary of Agriculture's final decision of salable quantity. (R. 119.) As stated, the Board had deliberated and made its

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<sup>1</sup> The Tax Court found that the Hop Control Board's recommendation for 1952 did not vary by more than one or two per cent from the Secretary's final decision (R. 116); but the determination which appears in the appendix to taxpayers' brief (pp. 24-27) shows that the Board's recommendation of salable quantity and the decision by the Secretary were identical (R. 105).

recommendation on July 17 for the year involved, 1952. (R. 116.) Obviously this was two weeks prior to July 31, 1952, which is the critical date here. In addition, decedent's son had special knowledge of market conditions during the time in question. Not only was he an experienced grower and dealer in hops but he was a member of the Hop Control Board, he participated in its deliberations during 1952 and he knew no later than July 17, 1952, that as a result of the Board's recommendation, approximately 35 per cent of the crop involved probably would be declared unsalable. (R. 57-58.) Thus, in view of the special knowledge of the growers and users of hops, manifestly salable quantity would obviously be an important factor in determining value on July 31, 1952.

The average market price for the type of hops involved as of the critical date, July 31, 1952, was between 49 and 52 cents per pound. In late August, when the hops involved matured, the price range was between 30 and 35 cents per pound.<sup>2</sup> From the

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<sup>2</sup> It might be pointed out that even in taxpayer's calculation (Br. 12), the market price of 49 cents is used despite the immaturity of the hops as of July 31, 1952. If the lower price range of 30 to 35 cents per pound was used, which would seem warranted since the hops did not mature until late August and early September (R. 115), a lower valuation, based upon market price, would result. Furthermore, the actual average price received was less than 49 cents per pound; it was 47.4 per pound, *excluding* the low sale price on the certificate purchase. Finally, the actual expense of harvesting and baling was 27.6 cents per pound (R. 113, 114), while 25 cents per pound is used in taxpayer's calculation (Br. 12).

middle of October through November the price range was between 45 and 50 cents per pound and during December the price range was between 50 and 53 cents per pound. (R. 115.)

Clearly, the evidence outlined above amply supports the Tax Court's finding that the fair market value of the hops as of July 31, 1952, was \$11,500 and we submit that such finding is not clearly erroneous. The Tax Court properly considered the maturity of the crop, the risk of loss, the estimated yield, the market price of similar hops, the cost of harvesting the matured crop, the salable quantity as restricted by the industry agreement, the special knowledge of buyers in the industry, and expert testimony. That these factors were appropriately taken into account is well established as confirmed by the Supreme Court in its statement in *Olson v. United States*, *supra*, p. 257:

In making that estimate [of market value] there should be taken into account all considerations that fairly might be brought forward and reasonably be given substantial weight in such bargaining [negotiations to determine fair sale price]. (Citation omitted.) The determination is to be made in the light of all facts affecting the market value that are shown by the evidence taken in connection with those of such general notoriety as not to require proof. \* \* \*

See also 10A Mertens, Law of Federal Income Taxation, Section 59.03 (1948 Rev. ed.); 2 Bonbright, Valuation of Property, pp. 1015-1018.

Of course, as this Court has stated in *Bank of California v. Commissioner*, 133 F. 2d 428, 432, the

weight to be given to various valuation factors is for the Tax Court to decide. *Elmhurst Cemetery Co. v. Commissioner, supra*, p. 40. It is the function of that tribunal to draw inferences, to weigh the evidence and declare the result. *Penn v. Commissioner, supra*, p. 20; *Elmhurst Cemetery Co. v. Commissioner, supra*, p. 40; *Helvering v. National Grocery Co.*, 304 U.S. 282, 295. Although taxpayer complains that the Tax Court did not accept its "expert" testimony (Br. 16-19), that tribunal is not obliged to accept as sound and blindly follow the opinion of any expert witness. *Penn v. Commissioner, supra*, p. 21; *Helvering v. National Grocery Co., supra*, p. 295; *Gloyd v. Commissioner*, 63 F. 2d 649, certiorari denied, 290 U.S. 633. To be bound, as taxpayer seemingly contends, would amount to the Tax Court's abdicating its function, namely, to find the facts. The Tax Court finds the facts—not the experts. *Gloyd v. Commissioner, supra*. Taxpayer only offered two experts, considering the evidence most favorably for taxpayer. One of these was an interested expert, the decedent's son who had managed the farm for many years. (R. 117.) Besides, the "expert opinion" offered was to the effect that such experts would not have sold the hops on the date involved for less than the cost of production (R. 47-48, 67), but the cost of production is only one factor in determining fair market value and, as the Supreme Court has stated (*Brooks-Scanlon Corp. v. United States*, 265 U.S. 106, 123) :

The value of property may be greater or less than its cost; and this is true of contract rights



and other intangibles as well as of physical things. \* \* \*

To be sure, the Tax Court cannot arbitrarily reject expert testimony. *Boggs & Buhl, Inc. v. Commissioner*, 34 F. 2d 859 (C.A. 3d); *Clinton Cotton Mills v. Commissioner*, 78 F. 2d 292 (C.A. 4th). However, there is adequate basis here, as previously shown by the evidence outlined, for the Tax Court's refusal to base its determination entirely on the opinion evidence of the experts offered by taxpayer. See *Tracy v. Commissioner*, 53 F. 2d 575 (C.A. 6th), certiorari denied, 287 U.S. 632.

Taxpayer contends that it was error for the Tax Court to base its finding on the fact that on July 31, 1952, it was known that not less than one-third of the crop could not be sold. (Br. 12-15.) However, it is crystal clear from the evidence that year after year the final determination of salable quantity by the Secretary did not vary substantially from the recommendation by the Board. (R. 116.) As pointed out, for the year involved, on July 17, the Board made its recommendation which ultimately was identical to the final determination. (R. 105.) Moreover, hop growers and dealers generally were aware of the Board's recommendation and of the likelihood of that recommendation being finally adopted. (R. 119.) In these circumstances, the effect of taxpayer's contention is to have the Tax Court disregard the obvious.

## CONCLUSION

The record fully supports the Tax Court's finding that the fair market value of the growing hops was \$11,500 on the critical date of July 31, 1952. Accordingly, the decision of the Tax Court is not clearly erroneous and should be affirmed.

Respectfully submitted,

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